

Written Statement to State of Nevada Department of Taxation
Committee on Local Government Finance – October 27, 2015

Re: Item 5 c): Report from subcommittee regarding guidance on enterprise funds and special revenue funds

TO: All Members of the Committee on Local Government Finance

FROM: Linda S. Newman, Homeowner Resident
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As an Incline Village homeowner and taxpayer I was interested to read the subcommittee's Guidance Letter 15-002 on the subject of Special Revenue and Enterprise Funds.

Our local government, the Incline Village General Improvement District, has recently adopted (effective July 1, 2015) Resolution No. 1838 which has created a series of new governmental type "special revenue" funds: Community Services Operations, Capital Projects and Debt Service; and, Beach Operations, Capital Projects and Debt Service. Prior to this resolution, the Community Services and Beach Funds existed for some number of decades as enterprise funds.

These funds conform to the NRS 354.517 definition for enterprise funds as they accounted for operations (1) which are financed and conducted in a manner similar to the operations of private business enterprises, where the intent of the governing body is to have the expenses (including depreciation) of providing goods or services on a continuing basis to the general public, financed or recovered primarily through charges to the users; or, (2) for which the governing body has decided that a periodic determination of revenues earned, expenses incurred and net income is consistent with public policy and is appropriate for capital maintenance, management control, accountability or other purposes.

The Community Services and Beach Funds conform to GASB Statement No. 34, Para 67 in that reported activities (golf, ski, tennis, multi-function recreation center, beaches) are financed through fees charged to external users for goods or services. In addition, "the pricing policies of the IVGID Board are designed to

recover all costs, including capital costs (such as depreciation or debt service) just as GASB Statement No. 34, Para 67(c) instructs.

I have serious concerns, based upon the subcommittee's Guidance Letter #15-002, that the current enterprise funds qualify as Special Revenue Funds.

I call the Committee's attention to the definition of Special Revenue Funds under GASB Statement No. 54, para 30 on page 4 of the Guidance Letter: "Special revenue funds are used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects. The term 'proceeds of specific revenue sources' establishes that one or more specific restricted or committed revenues should be the foundation for a special revenue fund. Those specific restricted or committed revenues may be initially received in another fund and subsequently distributed to a special revenue fund. **Those amounts should not be recognized as revenue in the fund initially receiving them; however, those inflows should be recognized as revenue in the special revenue fund in which they will be expended in accordance with specified purposes.**"

Here is the problem (actually, there are two). IVGID has approved the establishment of these Special Revenue Funds but it has not specified revenue which is restricted or committed to a specified purpose. All of the mandatory Recreation Facility Fees (close to \$7 million) have been allocated to the Community Service Fund and Beach Fund for operations –and according to the new 2015/16 District Budget these funds are reporting this inflow as revenue, despite the fact that GASB clearly states these "amounts should not be recognized as revenue in the fund initially receiving them;...those inflows should be recognized as revenue in the special revenue fund in which they will be expended in accordance with specified purposes." The District's original intent to change to Special Revenue was premised on the allocation of the Recreation Facility Fee into three components to ensure clarity and transparency. So the allocation was the purpose for the switch. However, no allocation was done; thus the entire Rec Fee is recorded in Revenues of the operating accounts of the Community Services and Beach Funds. This is contrary to its stated purpose.

Are these enterprise funds masquerading as special revenue funds? Or neither and not in compliance with NRS 354.472(1)(d) or NRS 354.612(2)?

Linda A. Newman

*Attached: Memorandum Dated December 1, 2014: From Gerald W. Eick, CPA CGMA; Director of Finance, Accounting, Risk Management and Information Technology to the Board of Trustees on Establishing Special Revenue, Capital Projects, and Debt Service funds, as well as related sub-funds for Community Services Fund and the Beach Fund, effective for July 1, 2015.

MEMORANDUM

TO: Board of Trustees

THROUGH: Steven J. Pinkerton
General Manager

FROM: Gerald W. Eick, CPA CGMA
Director of Finance, Accounting, Risk Management and Information Technology

SUBJECT: Establishing Special Revenue, Capital Projects, and Debt Service funds, as well as related sub-funds, for Community Services Fund and the Beach Fund, effective for July 1, 2015

DATE: December 1, 2014

I. RECOMMENDATION

That the Board of Trustees makes a motion to authorize Staff to assemble and report an Operating and Capital Budget for the fiscal year beginning July 1, 2015 to the State of Nevada Department of Taxation, Local Governments Division, that utilizes Special Revenue, Capital Project, and Debt Service Fund accounting for the Community Services Fund (which is comprised of the sub-funds Golf, Facilities, Ski, Recreation, Other Recreation, Parks and Tennis) and for the Beach Fund.

II. BACKGROUND

Staff has identified that the District's determination of fees and charges no longer is best reflected by an accounting under the Enterprise Fund format. The premise of Enterprise Funds is that pricing policies establish fees and charges designed to cover its costs including capital costs (such as depreciation or debt service). This premise will remain reasonably in place though the year ending June 30, 2015 to have continued to use and be consistent with our historical format. However, it is clear the magnitude of what the District does, as a responsible asset manager, requires the District to put as much planning and operating efforts into capital expenditure which in turn requires multi-year decision making and carries operating consequences. An example of such consequences is our building reserves for future projects. Another example is repurposing amounts that once were used to pay debt service to fund capital expenditures.

Measurement and reporting of these consequences no longer is served effectively by using the Enterprise Fund format however Utilities would continue as our only Enterprise Fund.

Accounting is both an art and a science. The science comes from the many standards that exist. For governments, it is mostly in the form of generally accepted governmental accounting principles. The art comes mostly in how information is assembled and communicated. Over the last few years, the District has set facility fees with stated elements for operations, capital, and debt, with an occasional eye to reserves. This has been done balancing the context of the total fee and long term capital expenditures and debt service and is as such identified, by the District, as "smoothing". We are pushing the definition for use of an Enterprise Fund. Our perspective is heavily affected by multi-year approach not a single operating period.

A number of community members have expressed frustration with not understanding our financial reports. Much of this complexity is caused by the standard by which Enterprise Funds report operations, which does not really reflect a flow of resources. A flow of resources format would ultimately make it clear how much goes to operations versus capital expenditure and debt service. That is why the District has presented budgets in two ways - based on operating results and Total Sources and Uses. However, despite a desire to provide maximum information, the result has been even greater confusion about why two budget formats.

Utilization of the Special Revenue Fund, which isolates operating revenues and expenditures, along with Capital Projects and Debt Service Funds, will allow the District to clearly identify the three main elements of the flow of transactions for Community Services and the Beach. Financial statement users, regulators, internal managers, and the public will all have one format and one consistent measurement of revenues and expenditures. Our internal management budgets, monthly reporting, audit reporting, and State budget document will be more concise and have a similar appearance. This simplicity and clarity alone justifies the change.

III. FINANCIAL IMPACT AND BUDGET

The effects of these changes are a matter of where transactions are reported. It does not change the total dollars. Many common elements of our current Total Sources and Uses budget would be used but will be separated by those which constitute Special Revenue (operations), versus Capital Projects, and Debt Service. Separation occurs both for revenue and expenditure. Under this model, the District would be able to demonstrate, through budgeting, accounting and reporting, the separate uses of the facility fee for operating, capital and debt. We have talked about it many times and presented it many ways in special reports, but we find users are still confused. Use of this new format would help to eliminate this confusion. Also, compliance with a restriction such as sales of coverage, which can only be used for capital, would be easier to identify and track over time, as would the accumulation of reserves for any category.

IV. ALTERNATIVES

The District could continue to utilize the Enterprise Fund format. Our auditors have acknowledged they can see both our current interpretation and our reasoning for change. They will support the change when we conclude it should be made. We are still close enough to either definition to consider both. However, as time progresses and we make more financial decisions with a longer view, the community will not be served either for understanding nor a reflection of what is occurring by using the Enterprise Fund format for Community Services and the Beach. Staff feels the change is inevitable and should be made now. We are already making multi-year decisions relative to capital plans. The change also minimizes the complexity and misunderstanding we have with those who read our reports. Not changing does not seem appropriate.

V. COMMENTS

Our new General Manager has many decades of experience with governmental accounting and reporting as a user. One of his first observations was why we were not utilizing Special Revenue Funds to report our Community Services and Beaches. Special Revenue Fund standards get its name from the recognition that governments often receive a revenue source for a particular purpose. Demonstrating compliance with both the measurements and the actual functional use of those revenues is an important part of the community's comfort with the

operation of its government. This is opportunity for the District to be clear and transparent with the flow of resources, how they are used, and because of the separate funds, also demonstrate a pattern of compliance, readiness or instances where these objectives are not met.

The District has recently upgraded its accounting system. During this process, Staff has already developed a revised chart of accounts that would facilitate the new funds. Also, for the last five years, under the current system, the Director of Finance has monitored a process by which all activity could be converted to the new format once the change is adopted. It may not be necessary to convert all years but it is possible if the need is determined. The most common use of historical data is the prior and current year comparison we use as we develop a future budget. We'd expect to convert the years ending June 30, 2014 and 2015 to facilitate the new budget.